

**UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF WISCONSIN**

UNITED STATES OF AMERICA,
Plaintiff,

v.

FRANKLIN ELECTRIC CO., INC.,
UNITED DOMINION INDUSTRIES LIMITED,

and

UNITED DOMINION INDUSTRIES, INC.,
Defendants.

Civil No:

Filed: 5/31/00

**MEMORANDUM OF UNITED STATES IN SUPPORT OF
MOTION FOR A TEMPORARY RESTRAINING ORDER
AND A PRELIMINARY INJUNCTION**

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I. Introduction

The United States brings this antitrust action to block the combination of Franklin Electric Co., Inc. (“Franklin Electric”) and United Dominion Industries, Inc. (“UDI”), the only two manufacturers of submersible turbine pumps for gasoline service stations (“STPs”) that are used in the United States. (United States’ Proposed Findings of Fact and Conclusions of Law [hereinafter “Prop. Find.”] ¶ 13.) Franklin Electric and UDI propose to combine their STP businesses into a new joint venture which will be controlled by Franklin Electric. (Prop. Find. ¶ 5.) The joint venture would eliminate the vigorous competition between the companies that has provided consumers with competitive prices, product innovation, and comprehensive service. (Prop. Find. ¶ 17.) Through the creation of the joint venture Franklin Electric would unlawfully gain monopoly power in the STP market, enabling the joint venture to raise prices and reduce quality and service.

STPs are a critical component in gasoline service stations. STPs are located in the underground gasoline storage tanks at service stations and pump the gasoline up through the piping system to the above-ground islands containing the dispensers¹ that ultimately deliver the gasoline to the vehicle. (Prop. Find. ¶ 7.) Currently, nearly all gasoline service stations in the United States require STPs for each of their underground storage tanks (Prop. Find. ¶ 11), and these purchasers of STPs have benefitted significantly from the competition between Franklin Electric and UDI (Prop. Find. ¶ 14). Defendants, for example, have made repeated improvements

¹ The dispenser contains the hose and nozzle for each grade of gasoline and is commonly called the “gas pump” by the general public. The actual pumping system is located in the underground storage tank, and not in the dispenser. Before STPs were developed and widely adopted, however, the pump was actually located in the dispenser and pulled the gasoline out of the storage tank by suction.

to their STPs, in significant part due to the competitive pressure created by their rivalry. (Prop. Find. ¶ 16.) The proposed joint venture would eliminate all competition in the STP market and give the joint venture significant market power — indeed, monopoly power — in violation of the antitrust laws.

Unless the Court issues the temporary restraining order and preliminary injunction requested by the United States, defendants may close this transaction as early as June 5, 2000, preventing a full and meaningful resolution of this case on the merits. To prevent serious harm to competition and to protect the service stations and other customers who are benefitting from competition between the merging firms, the United States has filed a complaint under § 7 of the Clayton Act. Section 7 provides that:

No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock . . . of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, *the effect of such acquisition may be substantially to lessen competition, or to tend to create an monopoly.*

15 U.S.C. § 18 (emphasis added). Plaintiff United States submits this Memorandum in support of its Motion for a Temporary Restraining Order and a Preliminary Injunction to prevent the defendants from consummating their proposed joint venture pending a full trial on the merits.

II. Factual Overview

A. The Defendants

1. Franklin Electric Co., Inc.

Franklin Electric is an Indiana corporation headquartered in Bluffton, Indiana. Franklin Electric is the world's largest manufacturer of submersible electric motors and a leading producer

of engineered specialty electric motor products and electronic drives and controls. In 1998, as part of the settlement of an intellectual property dispute between Franklin Electric and UDI, Franklin Electric purchased UDI's submersible motor business.

FE Petro, Inc. ("FE Petro") is a wholly-owned subsidiary of Franklin Electric; FE Petro's corporate headquarters is located in McFarland, Wisconsin. FE Petro was incorporated in July, 1988, and produced its first STP in late 1989 after acquiring the STP business of Gilbarco. Its STPs are sold under the "FE Petro" brand name. In November, 1992, FE Petro also acquired the STP business of Tokheim Corporation. FE Petro produces STPs in its plant in McFarland, Wisconsin, using motors that Franklin Electric manufactures in Bluffton, Indiana. Franklin Electric will likely close the McFarland plant if it succeeds in acquiring control over the Marley STP business.

2. United Dominion Industries Limited and United Dominion Industries, Inc.

United Dominion Industries Limited is a Canadian corporation headquartered in Charlotte, North Carolina. The company manufactures proprietary engineered products for industrial markets throughout the world. UDI, a wholly-owned subsidiary of United Dominion Industries Limited, is a Delaware corporation also headquartered in Charlotte, North Carolina. Marley Pump Company ("Marley Pump"), a division of UDI, is a Delaware corporation headquartered in Davenport, Iowa. UDI acquired The Marley Company ("Marley"), including its Marley Pump subsidiary, in 1993. Marley designs, manufactures, and sells STPs, mechanical and electronic leak detection devices, and submersible and surface pump water systems. Marley Pump's products are sold under the "Red Jacket" brand name. Marley Pump manufactures its STPs in Davenport,

Iowa.

B. The Proposed Transaction

Pursuant to a joint venture agreement between Franklin Electric and UDI, Franklin Electric will contribute 100% of the voting stock of FE Petro to the joint venture. UDI will contribute the principal assets used in its STP business to the joint venture. Franklin Electric will own 75% of the joint venture and therefore control the joint venture's operations; UDI will own the remaining 25%. On formation of the joint venture, Franklin Electric will pay UDI approximately \$50.3 million. Under the terms of the joint venture agreement, Franklin Electric can force UDI to sell its share of the joint venture at any time for \$16.8 million; UDI can also force Franklin Electric to purchase UDI's share of the joint venture at any time, also for \$16.8 million.

C. The Submersible Turbine Pump Industry

A submersible turbine pump is an essential piece of equipment in gasoline service stations in the United States. As the name suggests, the pump is submersed in gasoline inside the underground storage tank. One STP is required for each storage tank at a gasoline service station. For example, a typical gasoline service station might have three STPs: one for standard-grade gasoline, one for high-grade gasoline, and one for diesel fuel.² An STP can generally be purchased for under \$1500.

An STP consists of three main components: a motor, a pumping unit, and a discharge head. In appearance, an STP resembles a pipe with a slightly larger cylinder at the bottom and the

² Some service stations blend the standard-grade and high-grade fuels at the dispenser to create a medium-grade fuel. Other service stations maintain a separate storage tank (and STP) for a medium-grade fuel.

distribution head at the top. The underground storage tanks typically have an opening just large enough to insert a motor and pumping unit four inches in diameter. The cylinder, which extends vertically from an opening at the top of the storage tank to just a few inches from the bottom, contains the actual pumping unit, the electric motor, and the impeller, which forces the gasoline up through the cylinder. The distribution head, which sits on top of the tank, contains the manifold and connects to the underground network of pipes. The distribution head also contains the electrical supply; a conduit extending through the cylindrical pipe contains wires that supply power to the pumping mechanism.

STPs come in a variety of motor horsepowers and are increasingly equipped with variable speed and telescoping shaft features. Variable speed drives allow the pump to maintain a constant flow regardless of the number of dispensers delivering gas from that storage tank at any particular time. The telescoping shaft allows the product to be adjusted to fit a variety of underground storage tanks.

Because the pump in an STP operates while submerged in gasoline, it must be designed so that it does not produce sparks that would ignite the gasoline and cause an explosion. In the United States, STPs must therefore receive Class I explosion proof certification from Underwriter Laboratories (“UL”). (Prop. Find. ¶ 9.) UL certification requires that the pump’s motor be sealed away from the gasoline in which it rests, and that the electrical connection, wiring, and other components have gasoline resistant properties. Franklin Electric is the only company in the world that manufactures submersible motors that are approved by UL for sale in the United

States.³ (Prop. Find. ¶ 23.)

FE Petro and Marley sell their STPs primarily through independent petroleum equipment distributors. These independent distributors sell a wide range of petroleum equipment to gasoline service station owners, operators, and building contractors. A small portion of STPs are sold directly to FE Petro's and Marley's larger end-user customers, including major oil companies such as ExxonMobil or BP Amoco. The major oil companies, however, operate only a fraction of the stations which market gasoline under their brand name. The remaining stations are owned by independent firms; these firms purchase STPs independently and are not bound by the major oil companies' decision to purchase a particular brand STP.

The only product that can perform the same general function as an STP — moving the gasoline from the underground storage tank to the dispenser — is the suction pump. Suction pumps are located inside each gasoline dispenser instead of in the underground storage tank. Because a single STP can serve several dispensers, STPs have virtually replaced suction pumps for use in gasoline service stations in the United States. Suction pumps are still used in commercial applications, such as a business with an on-site dispenser to service its own fleet of trucks.

FE Petro and Marley are the only two manufacturers in the world of STPs suitable for use in the United States.⁴ (Prop. Find. ¶ 13.) Competition between FE Petro and Marley has

³ UDI manufactured UL-approved submersible motors until 1998, when it sold its submersible motor business to Franklin Electric and entered into a ten year motor supply agreement with Franklin Electric.

⁴ Barbero, a small Italian firm, manufactures STPs that are not approved by UL. Barbero has less than 1% of the worldwide sales of STPs. FE Petro and Marley account for more than 99% of STP sales worldwide.

provided tremendous benefits to customers, particularly in terms of price, innovation, and service. (Prop. Find. ¶ 14.) Before FE Petro entered the market, Marley Pump was the dominant supplier of STPs in the United States and the world. Because customers had few choices for STPs, competition in pricing, service, and product innovation was minimal. As a new entrant, FE Petro struggled for years until it introduced two major improvements to the STP: a variable speed drive and a telescoping shaft. Both these features developed by FE Petro had enormous appeal to customers. As a result of this innovation, FE Petro rapidly gained market share and Marley was ultimately forced to copy these improvements to remain competitive. FE Petro developed a variable speed motor that improved flow to the dispenser in large gasoline service stations. FE Petro also developed a telescoping, or variable-length, shaft for the STP. The telescoping shaft makes the installation of STPs easier, since the piping can be adjusted to fit different size tanks; the telescoping STP is also easier to transport and store because it takes up less space.

III. The Legal Standard for Preliminary Relief Has Been Satisfied

Pursuant to § 15 of the Clayton Act, in proceedings brought by the United States to prevent the Act's violation, "the court may at any time make such temporary restraining order or prohibition as shall be deemed just in the premises." 15 U.S.C. § 25.

The standard employed in the Seventh Circuit for granting preliminary relief⁵ requires the movant to "meet the threshold burden of establishing (1) some likelihood of prevailing on the merits; and (2) that in the absence of the injunction, [the movant] will suffer irreparable harm for which there is no adequate remedy at law." *AlliedSignal, Inc. v. B.F. Goodrich Co.*, 183 F.3d

⁵ The standards for issuing a temporary restraining order and a preliminary injunction are the same in the Seventh Circuit. *See, e.g., YourNetDating, LLC v. Mitchell*, 88 F. Supp. 2d 870, 871 (N.D. Ill. 2000).

568, 573 (7th Cir. 1999). Once the movant satisfies this initial test, the district court “engages in a ‘sliding scale’ analysis by balancing the harms to the parties and the public interest.” *Id.* The Seventh Circuit has described this sliding scale analysis in antitrust cases by observing that “[t]he greater the plaintiff’s likelihood of success on the merits when those merits are ultimately determined after a full trial . . . the less harm from denial of the preliminary injunction the plaintiff need show in relation to the harm that the defendant will suffer if the preliminary injunction is granted.” *FTC v. Elders Grain, Inc.*, 868 F.2d 901, 903 (7th Cir. 1989).

The application of this test in the present case leads to the inexorable conclusion that preliminary relief should issue. First, the United States can demonstrate overwhelmingly that the proposed transaction, which will eliminate Franklin Electric’s only competitor in the STP market, is likely to substantially lessen competition in the STP market, and thus that the proposed transaction violates § 7 of the Clayton Act. Second, once the United States shows a reasonable probability that § 7 has been violated, the government “need not prove irreparable injury to obtain a preliminary injunction.” *Elders Grain*, 868 F.2d at 903; *accord FTC v. World Travel Vacation Brokers, Inc.*, 861 F.2d 1020, 1028-29 (7th Cir. 1988); *United States v. Siemens Corp.*, 621 F.2d 499, 506 (2d Cir. 1980); *United States v. Ingersoll-Rand Co.*, 320 F.2d 509, 524 (3d Cir. 1963). Third, although the defendants may claim that they will suffer financial harm as a result of any delay in closing the transaction, any such harm is speculative in nature and does not outweigh the public’s interest in preserving competition in the present case. *See Elders Grain*, 868 F.2d at 903-04. Fourth, maintenance of the status quo through the issuance of preliminary relief comports with Congress’ intent in enacting the Clayton Act, and thus is in the public interest. *See Gulf & W. Indus. v. Great Atl. & Pac. Tea Co.*, 476 F.2d 687, 699 (2d Cir. 1973) (noting that in

litigation brought by the government, any “doubts as to whether an injunction sought is necessary to safeguard the public interest — when the public interest involved is as clear, pervasive and vital as the record here demonstrates — should be resolved in favor of granting the injunction” (citing *United States v. First Nat’l City Bank*, 379 U.S. 378, 383 (1965))).

A. The Government Is Likely to Succeed on the Merits Under the Standards Established by § 7 of the Clayton Act

Section 7 of the Clayton Act prohibits any acquisition “where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.” 15 U.S.C. § 18. The purpose of § 7 is to prevent acquisitions or mergers *before* they create harm. See *Brown Shoe Co. v. United States*, 370 U.S. 294, 318 n.32 (1962); *Hospital Corp. of Am. v. FTC*, 807 F.2d 1381, 1389 (7th Cir. 1986); *Fruehauf Corp. v. FTC*, 603 F.2d 345, 351 (2d Cir. 1979) (noting that “Section 7 of the Clayton Act was intended to arrest a trade restraint or a substantial lessening of competition in its incipiency; it is not concerned with ‘certainties’”).

To establish a § 7 violation, a “plaintiff need only prove that [the] effect [of the challenged acquisition] ‘*may be* substantially to lessen competition’” within a relevant market. *California v. American Stores Co.*, 495 U.S. 271, 284 (1990) (quoting 15 U.S.C. § 18) (emphasis added in original). Accordingly, “[s]ection 7 does not require proof that a merger or other acquisition has caused higher prices in the affected market. All that is necessary is that the merger create an appreciable danger of such consequences in the future. A predictive judgment, necessarily probabilistic and judgmental rather than demonstrable is called for.” *Hospital Corp.*, 807 F.2d at 1389 (citation omitted) (citing *United States v. Philadelphia Nat’l Bank*, 374 U.S. 321, 362

(1963)); accord *FTC v. PepsiCo*, 477 F.2d 24, 28 (2d Cir. 1973) (noting that the government “need not establish any actual anti-competitive effects but only an incipency”). “[D]oubts are to be resolved against the transaction.” *Elders Grain*, 868 F.2d at 906.

To predict whether an acquisition may substantially lessen competition or tend to create a monopoly, the reviewing court must determine: (1) the “line of commerce” or product market in which to assess the transaction; (2) the “section of the country” or geographic market in which to assess the transaction, and (3) the transaction’s probable effect on competition in the product and geographic markets. See *United States v. Marine Bancorporation*, 418 U.S. 602, 618-23 (1974); *FTC v. Cardinal Health, Inc.*, 12 F. Supp. 2d 34, 45 (D.D.C. 1998); *United States v. Ivaco, Inc.*, 704 F. Supp. 1409, 1415, 1418 (W.D. Mich. 1989); *Christian Schmidt Brewing Co. v. G. Heileman Brewing Co.*, 600 F. Supp. 1326, 1328 (E.D. Mich.), *aff’d*, 753 F.2d 1354 (6th Cir. 1985). The Seventh Circuit has mandated that “the economic concept of competition, rather than any desire to preserve rivals as such, is the lodestar that shall guide the contemporary application of the antitrust laws,” including in merger cases.⁶ *Hospital Corp.*, 807 F.2d at 1386.

1. The Government Is Likely to Prevail at Trial in Establishing That the Production, Manufacture, and Sale of Submersible Turbine Pumps Is a Relevant Product Market

a. Relevant Product Markets Include All Practical, Cost-Effective Substitutes and Exclude Other Possible Substitutes

The starting point in any merger analysis is determining the relevant product market. The

⁶ The Seventh Circuit has also observed that “[w]hen an economic approach is taken in a section 7 case, the ultimate issue is whether the challenged acquisition is likely to facilitate collusion.” *Hospital Corp.*, 807 F.2d at 1386. A merger to monopoly represents the ultimate facilitation of collusion by eliminating the need for collusion entirely — if the proposed joint venture is consummated, there will be no one left that Franklin Electric must collude with in order to raise prices.

relevant product market establishes the boundaries within which competition meaningfully exists. Those “commodities reasonably interchangeable by consumers for the same purposes” constitute a product market for antitrust purposes. *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 395 (1956). As the Supreme Court has recognized, the market “must be drawn narrowly to exclude any other product to which, within reasonable variations in price, only a limited number of buyers will turn.” *Times-Picayune Publishing Co. v. United States*, 345 U.S. 594, 612 n.31 (1953); *accord Brown Shoe*, 370 U.S. at 325 (noting that product markets are delineated “by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it”).

A way of verifying whether substitutes are practical and cost effective, and therefore belong in the product market, is by ascertaining whether an increase in price for the product in question would cause a sufficient number of buyers to turn to other product substitutes so as to make the price increase unprofitable. *See United States v. Archer-Daniels-Midland Co.*, 866 F.2d 242, 246-48 (8th Cir. 1988). If the price increase would be profitable, despite the availability of the claimed substitutes, those other product substitutes are properly excluded from the relevant product market. *See id.* at 248.

This same analytical approach is incorporated into the Department of Justice and Federal Trade Commission 1992 Horizontal Merger Guidelines. *See* U.S. Department of Justice and Federal Trade Commission, *Horizontal Merger Guidelines* ¶ 1.11 (1997 rev.) (hereinafter “Merger Guidelines”).⁷ The Merger Guidelines take the smallest possible group of competing

⁷ Courts often look to the Merger Guidelines’ analytical approach to define markets. *See, e.g., Ball Memorial Hosp., Inc. v. Mutual Hosp. Ins., Inc.*, 784 F.2d 1325, 1336 (7th Cir. 1986); *Community Publishers, Inc. v. Donrey Corp.*, 892 F. Supp. 1146, 1153 n.6 (W.D. Ark.

products and ask whether a “hypothetical monopolist over that group of products would profitably impose at least a ‘small but significant and nontransitory’ [price] increase.” Merger Guidelines ¶ 1.11. Under the Merger Guidelines, a “small but significant and nontransitory” price increase in most instances is an “increase of five percent lasting for the foreseeable future.” *Id.* ¶ 1.11; accord *Consolidated Gold Fields, PLC v. Anglo Am. Corp. of S. Afr.*, 698 F. Supp. 487, 501 (S.D.N.Y. 1988) (noting that the “benchmark for including a substitute in a market is that the sales of the substitute rise significantly in response to a non-temporary 5% or more increase in prices”), *aff’d in part and rev’d in part on other grounds sub nom. Consolidated Gold Fields PLC v. Minorco, SA*, 871 F.2d 252 (2d Cir. 1989).

b. The Development, Production, and Sale of Submersible Turbine Pumps Constitutes a Relevant Product Market

In the event of a small but significant increase in the price of STPs, gasoline service stations would not switch to any other product in sufficient numbers to defeat the profitability of the price increase. (Prop. Find. ¶ 12.) No other product is an effective economic substitute for STPs in the United States. (Prop. Find. ¶ 11.) While suction pumps can deliver fuel from underground storage tanks to the dispenser, as STPs do, suction pumps suffer from several performance and financial disadvantages that make them a poor economic substitute for STPs in the large, high-volume service stations prevalent in the United States.

Suction pumps cannot be used in large modern service stations because they cannot effectively pull the gasoline with the required flow rate for the distance required under the layout

1995) (“It is well recognized that the Merger Guidelines do not have the force of law, but many courts still cite them, and the expert testimony in this case shows that they represent mainstream economic thinking.” (citation omitted)), *aff’d sub nom. Community Publishers, Inc. v. DR Partners*, 139 F.3d 1180 (8th Cir. 1998).

of modern stations with large underground storage tanks. Suction pumps are also more expensive in a high-volume retail service station because far more suction pumps would be needed. A separate suction pump is needed in each dispenser for each grade of gasoline, whereas a single STP in the underground storage tank can serve all the dispensers connected to that tank. In addition, substantially more piping may be required in a suction pump system than in an STP system. Suction pumps are also subject to “vapor lock” at high temperatures; vapor lock shuts down the pump and occurs when the fuel vaporizes due to the heat and the suctioning force applied by the suction pump.

In a retail service station, where STPs are primarily used today, the economics of the STP are so compelling in comparison to the suction pump that consumers would not switch to suction pumps in response to a small but significant increase in the price of STPs, nor would STP purchasers refrain from buying STPs in response to a small but significant non-transitory price increase. While STPs represent a very small portion of the cost of building, upgrading, and operating a gasoline service station, STPs are a critical component of any gas station. A modest increase in the price of STPs would therefore have little, if any, impact on the demand for STPs. Demand for STPs is, in other words, highly inelastic.

2. The Government Is Likely to Prevail at Trial in Establishing That the United States Is a Relevant Geographic Market for the Manufacture and Sale of Submersible Turbine Pumps

A relevant geographic market is an “area in which the seller operates, and to which the purchaser can practicably turn for supplies.” *United States v. Philadelphia Nat’l Bank*, 374 U.S. 321, 359 (1963) (internal quotation marks and emphasis omitted); *accord Elders Grain*, 868 F.2d at 907 (“A market is the set of sellers to which a set of buyers can turn for supplies at existing or

slightly higher prices”). If consumers in a given geographic area do not consider products from outside that area as reasonable, practical alternatives, then that geographic area is a relevant geographic market. *Hospital Corp.*, 807 F.2d at 1388. The Merger Guidelines identify the relevant geographic market as “a region such that a hypothetical monopolist that was the only present or future producer of the relevant product at locations in that region would profitably impose at least a ‘small but significant and nontransitory’ increase in price, holding constant the terms of sale for all products produced elsewhere.” Merger Guidelines ¶ 1.21.

For submersible turbine pumps, the relevant geographic market is the United States. FE Petro and Red Jacket STPs are manufactured in the United States and sold throughout the United States. Currently, there are no STPs manufactured abroad that are imported for use in the United States. The government is aware of only one firm outside the United States — Barbero, a small Italian company — that manufactures STPs. Barbero has less than a 1% share of worldwide STP sales and its STP has not been approved by UL for sale in the United States. U.S. STP customers would therefore not turn to Barbero in response to a price increase by a hypothetical monopolist in the United States. Accordingly, the United States is a relevant geographic market for the production and sale of STPs.

3. The Government Is Likely to Prevail at Trial in Establishing that the Acquisition Is Likely to Lessen Competition Substantially

a. The Transaction Creating a Joint Venture with Control of All of the Submersible Turbine Pump Market Is Presumptively Illegal

A transaction challenged under § 7 of the Clayton Act is *presumed* illegal if the Government can show that the combined entity would have a significant market share in a

sufficiently concentrated market. *Philadelphia Nat'l Bank*, 374 U.S. at 363 (concluding that “a merger which produces a firm controlling an undue percentage share of the relevant market, and results in a significant increase in the concentration of firms in that market is so inherently likely to lessen competition substantially that it must be enjoined in the absence of evidence clearly showing that the merger is not likely to have such anticompetitive effects”); *United States v. Rockford Memorial Corp.*, 898 F.2d 1278, 1285 (7th Cir. 1990); *see also FTC v. University Health, Inc.*, 938 F.2d 1206, 1218 (11th Cir. 1991). In *Philadelphia National Bank*, the Supreme Court held that a merger resulting in a single firm controlling 30% of a market in which four firms had 78% of the sales was presumptively illegal. *Philadelphia Nat'l Bank*, 374 U.S. at 364. Similarly, in *United States v. Continental Can Co.*, 378 U.S. 441 (1964), the Court found a merger presumptively illegal where the merging firms’ aggregate market share was 25%, the acquired firm’s pre-merger share was 3.1%, and the leading four firms would have accounted for 66.8% of the relevant market after the merger. *Id.* at 461.⁸

⁸ A growing number of courts, including those in the Seventh Circuit, have applied the Merger Guidelines’ approach for assessing pre- and post-merger concentration through use of the Herfindahl-Hirschman Index (“HHI”). *See, e.g., Allied Signal*, 183 F.3d at 574. The HHI for a market is calculated by summing the squares of the individual market shares of all firms participating in the market. Merger Guidelines ¶ 1.5.

Under the Merger Guidelines’ approach, markets with an HHI below 1000 are deemed “unconcentrated;” those with an HHI between 1000 and 1800 are “moderately concentrated;” and those with an HHI above 1800 are termed “highly concentrated.” *Id.* ¶ 1.51. In cases where the post-merger market is “highly concentrated,” and an acquisition would result in an increase of more than 100 points in the HHI, the acquisition is presumed to be “likely to create or enhance market power or facilitate its exercise.” *Id.* ¶ 1.51(c).

Although the Merger Guidelines’ standards for creating a presumption that a transaction is anticompetitive have been called overly strict, “in the sense of erring on the side of allowing takeovers to proceed,” *Consolidated Gold Fields*, 698 F. Supp. at 500, the acquisition in this case far exceeds even these conservative standards. Franklin Electric’s acquisition of control over the Marley STP business would increase the HHI in the United States STP market, based on 1999 sales figures, by 4838 points, from 5162 to the maximum of 10,000.

Here the parties are merging to monopoly. The joint venture would eliminate the vigorous competition that exists today between FE Petro and Marley. This market has been served by a monopoly firm in the past; Marley's dominant position before FE Petro's entry into the market resulted in uncompetitive pricing, poor service, and minimal innovation. If defendants are allowed to proceed with the proposed joint venture, Franklin Electric would control 100% of the United States market for STPs. Following the Supreme Court's mandate in *Philadelphia National Bank*, the proposed transaction must be presumed illegal. *See also Rockford Memorial*, 898 F.2d at 1285-86.

b. The Defendants Cannot Point to Any Factors That Overcome the Presumption That the Proposed Joint Venture is Illegal

Once the United States has established a presumptive violation of the Clayton Act, the defendants may introduce evidence to attempt to rebut that presumption. However, the Supreme Court has directed that the presumption will not easily be overcome. *Philadelphia Nat'l Bank*, 374 U.S. at 363 (concluding that defendants must "clearly" demonstrate that the acquisition will not substantially lessen competition). Defendants can only rebut this presumption of illegality by a clear showing that other market characteristics would preclude the merger from substantially lessening competition. *Id.*; *United States v. General Dynamics Corp.*, 415 U.S. 486, 497-98 (1974). In such a case, the presumption of illegality can be overcome only if the defendants show that "the market-share statistics gave an inaccurate account of the acquisition['s] probable effects on competition." *United States v. Citizens & S. Nat'l Bank*, 422 U.S. 86, 120 (1975); accord *Rockford Memorial*, 898 F.2d at 1286 (noting that once government established merger would create firm with monopoly market share, "it behooved the defendants to present evidence that the

normal inference to be drawn from such a market share would mislead”).

(1) Entry Is Not Likely to Occur in a Timely and Sufficient Manner to Prevent Franklin Electric from Exercising Market Power

The presumption that the proposed transaction will result in anticompetitive effects, created by Franklin Electric’s control of the entire STP market after the joint venture, can generally be overcome where entry in the market is so easy that the merged entity could not profitably maintain a price increase above pre-merger levels. *See, e.g., United States v. Baker Hughes Inc.*, 908 F.2d 981, 987 (D.C. Cir. 1990) (“In the absence of significant [entry] barriers, a company probably cannot maintain supracompetitive pricing for any length of time.”); *Will v. Comprehensive Accounting Corp.*, 776 F.2d 665, 672 n.3 (7th Cir. 1985) (“Unless barriers to entry prevent rivals from entering the market at the same cost of production, even a very large market share does not establish market power.”); *cf. Elders Grain*, 868 F.2d at 905 (concluding that “since entry into the industry is slow,” collusion could be profitable). However, whether entry is sufficiently easy to eliminate the anticompetitive danger posed by a given transaction will depend on whether such entry would be timely, likely and sufficient in its magnitude, character and scope to deter or counteract the loss of competition. *See, e.g., Merger Guidelines* ¶ 3.0. Thus, the question of whether entry can rebut a prima facie showing that a transaction violates Section 7 turns on the specific facts of the particular market affected by the transaction. *See, e.g., Tasty Baking Co v. Ralston Purina, Inc.*, 653 F. Supp. 1250, 1263-64 (E.D. Pa. 1987); *cf. Ball Memorial Hosp., Inc. v. Mutual Hosp. Ins., Inc.*, 784 F.2d 1325, 1335-37 (7th Cir. 1986) (concluding in rule of reason case that low entry barriers in particular market overcame usual inference of market power from high market share figures).

In the STP market, substantial entry is unlikely to occur within a sufficient period of time to discipline the merged firm. Any new entrant would face substantial difficulties, including the necessity of designing around patents that would be held by Franklin Electric,⁹ locating a source of motors for the pump,¹⁰ securing approval from the UL, establishing a distribution network, and obtaining customer acceptance of the new product, all in the face of established products currently produced by the defendants. Even from the perspective of the most optimistic new entrant, it would be at least three years before the new entrant has any substantial share of the STP market.¹¹ Any new entrant, moreover, would be forced to compete with an entrenched monopolist, further reducing the likelihood the entrant would be a viable competitor. The likelihood of a new firm entering the STP market in a timely and sufficient manner to prevent Franklin Electric from exercising market power through the joint venture is exceedingly remote.

(2) Defendants Cannot Demonstrate That the Anticompetitive Effects of the Transaction Are Overcome by Countervailing Efficiencies

Although Franklin Electric may claim that the acquisition of control over its only competitor would result in efficiencies, such efficiencies do not justify approval of this merger to

⁹ The patents cover key competitive features such as the variable speed drive and the telescoping shaft. Franklin Electric has been vigorous in defending its patents in the past — witness the recent STP patent litigation between Franklin Electric and Marley.

¹⁰ Franklin Electric is the only company that currently manufactures motors that can be used in petroleum STPs in the United States. Finding an alternative source for the motor would likely be difficult, time-consuming, and expensive.

¹¹ It took FE Petro at least five years to achieve a substantial market share; FE Petro only began to truly succeed when it introduced innovative technology that offered clear benefits to the consumer. FE Petro was also able to facilitate its entry by purchasing smaller STP manufacturers that existed in the market at the time. If the defendants succeed in creating their proposed joint venture, a new entrant would not be able to acquire this foothold.

monopoly. Case law suggests that claimed efficiencies cannot save an otherwise illegal merger:

[A] merger the effect of which “may be substantially to lessen competition” is not saved because, on some ultimate reckoning of social or economic debits and credits, it may be deemed beneficial. A value choice of such magnitude is beyond the ordinary limits of judicial competence, and in any event has been made for us already, by Congress when it enacted the amended § 7. Congress determined to preserve our traditionally competitive economy.

Philadelphia Nat’l Bank, 374 U.S. at 371; *accord FTC v. Procter & Gamble Co.*, 386 U.S. 568, 580 (1967); *United States v. United Tote, Inc.*, 768 F. Supp. 1064, 1084-85 (D. Del. 1991) (noting that “even if the merger resulted in efficiency gains, there are no guarantees that these savings would be passed on to the consuming public”); *United States v. Rockford Memorial Corp.*, 717 F. Supp. 1251, 1288-89 (N.D. Ill. 1989), *aff’d*, 898 F.2d 1278 (7th Cir. 1990); *United Nuclear Corp. v. Combustion Eng’g, Inc.*, 302 F. Supp. 539, 554-555 (E.D. Pa. 1969). Indeed, no court has ever approved a merger based on an efficiencies defense, let alone in a merger to monopoly.

The Merger Guidelines allow for consideration of verifiable, merger-specific efficiencies that are generated in the relevant product market, if the “efficiencies are of a character and magnitude such that the merger is not likely to be anticompetitive in any relevant market.” Merger Guidelines ¶ 4. The Merger Guidelines, however, correctly caution that “[e]fficiencies almost never justify a merger to monopoly or near-monopoly.” *Id.* This merger does not present the exceptional case where a merger to monopoly might be justified by substantial and credible claims of merger-specific efficiencies. Even courts that have considered efficiency claims have laid down a “very rigorous standard” that must be met. *Rockford Memorial*, 717 F. Supp. at 1289. Defendants must prove, by “clear and convincing evidence,” *id.*, that their claimed

efficiencies: (1) will actually be achieved and are not based on speculation, *University Health*, 938 F.2d at 1222-23; (2) are merger specific, and can be achieved “only through the merger and in no other manner,” *Rockford Memorial*, 717 F. Supp. at 1289; (3) will be passed on, providing a “significant economic benefit to consumers,” *id.*; and (4) will outweigh the merger’s anticompetitive effect, providing a “net economic benefit” for the consumer, *id.* at 1291.

Franklin Electric cannot meet this demanding standard. Franklin Electric did not conduct a detailed analysis of the cost savings that could be achieved by the joint venture prior to entering into the joint venture agreement. Franklin Electric has offered only broad estimates that are unaccompanied by the details necessary to conclude the savings will be achieved. Nor is it possible to conclude that these savings, given their speculative and vague contours, can only be achieved through the combination of the STP businesses of Franklin Electric and UDI.

More importantly, given the extremely high inelasticity of demand for STPs there is no reason to believe any efficiencies Franklin Electric managed to achieve through the joint venture would be passed on to the customer. The monopolistic joint venture would have no incentive to lower prices as doing so would not substantially increase demand for STPs; conversely, Franklin Electric, as a monopolist, would have every incentive to raise price as doing so would not reduce demand.

Defendants have claimed they need to merge in order to penetrate the markets outside the United States that, for a variety of historical reasons, largely still rely on suction pumps. The defendants have not established that they need to merge their businesses in order to develop these new markets; indeed, both FE Petro and Marley sell their products throughout the world today. Even if the defendants’ argument were true, however, customers in the United States should not

be forced to endure a monopolist in STPs so that customers in other countries can benefit.

Philadelphia Nat'l Bank, 374 U.S. at 370 (rejecting argument that “anticompetitive effects in one market could be justified by procompetitive consequences in another”).

B. In the Absence of Injunctive Relief Competition Will Suffer Irreparable Harm

Once the government has established a likelihood of success on the merits of its § 7 claim, irreparable harm is presumed. *Elders Grain*, 868 F.2d at 903. This is so because “the threatened violation of the law here is itself sufficient public injury to justify the requested relief. The Congressional pronouncement in § 7 embodies the irreparable injury of violations of its provisions.” *United States v. Ingersoll-Rand Co.*, 218 F. Supp. 530, 544 (W.D. Pa.), *aff'd*, 320 F.2d 509 (3d Cir. 1963); *accord Ivaco*, 704 F. Supp. at 1429.

In this instance, serious and permanent harm to competition would occur if the transaction is allowed to proceed. Once the assets of the two firms are combined to form the joint venture, management, manufacturing, marketing and service personnel are integrated, and customer and trade relationships are rearranged, it becomes unlikely that even a subsequent divestiture would adequately return the market to its pre-merger state. In addition, competition would be harmed substantially in the interim.

Courts have long recognized that an after-the-fact, court-ordered divestiture is most often an inferior alternative to preliminary relief. “If preliminary relief is not awarded and the merger is subsequently found to be unlawful, it would be extremely difficult, if at all possible, to remedy effectively the unlawful merger.” *Christian Schmidt Brewing*, 600 F. Supp. at 1332; *Ivaco*, 704 F. Supp. at 1429 (concluding that subsequent divestiture requirements are “typically rejected by

the courts as ineffective.”). Nor would any form of preliminary relief less than a complete injunction be adequate. A hold separate order, no matter how well crafted, would not protect the public against interim competitive harm or ensure the adequacy of final relief. *See FTC v. PPG Indus.*, 798 F.2d 1500, 1507-08 (D.C. Cir. 1986); *United States v. White Consol. Indus.*, 323 F. Supp. 1397, 1399 (N.D. Ohio 1971); *United States v. Wilson Sporting Goods Co.*, 288 F. Supp. 543, 569 (N.D. Ill. 1968); *cf. AlliedSignal*, 183 F.3d at 576 (concluding that district court judge did not abuse discretion in issuing preliminary injunction where defendant offered to hold division of company separate, as “this might unduly prejudice the scope of a possible remedy should the merger ultimately be found to violate Section 7”). In cases such as this, where the transaction is “almost certainly illegal, the district court face[s] a difficult task in justifying anything less than a full stop injunction.” *PPG Indus.*, 798 F.2d at 1506 (assessing case under statutory preliminary injunction standard of § 13(b) of the FTC Act); *see also FTC v. Staples, Inc.*, 970 F. Supp. 1066, 1091 (D.D.C. 1997) (employing § 13(b) standard and stating that where “the Court finds that the [government] has established a likelihood of success on the merits, a presumption in favor of a preliminary injunction arises”). Unless a temporary restraining order and preliminary injunction are issued, purchasers of STPs will suffer irreparable harm.

C. Preliminary Relief Advances the Public Interest

Preservation of FE Petro and Marley as independent competitors is also in the public interest. “By enacting Section 7, Congress declared that the preservation of competition is always in the public interest.” *Ivaco*, 704 F. Supp. at 1430; *accord Marathon Oil Co. v. Mobil Corp.*, 530 F. Supp. 315, 320 (N.D. Ohio) (“[T]he mere possibility that Marathon would be eliminated as an effective competitor from the marketplace is sufficient to satisfy the public interest criterion.”),

aff'd, 669 F.2d 378 (6th Cir. 1981). “The public has an interest in the preservation of competition in the market, and an injunction is necessary to protect that interest.” *Ivaco*, 704 F. Supp. at 1430. An injunction would preserve competition between FE Petro and Marley in the STP market.

D. Any Pecuniary Harm to the Defendants’ Interests Is Outweighed by the Public’s Interest in Preserving Competition

Although the issuance of a preliminary injunction would delay closing of the proposed transaction, and perhaps cause the defendants some risk of pecuniary harm, “[t]his private, financial harm must, however yield to the public interest in maintaining effective competition.” *Ivaco*, 704 F. Supp. at 1430; *accord Elders Grain*, 868 F.2d at 903; *University Health*, 938 F.2d at 1225; *Christian Schmidt Brewing*, 600 F. Supp. at 1332; *United States v. Columbia Pictures Indus.*, 507 F. Supp. 412, 434 (S.D.N.Y. 1980).

The interest of the public here is great since lessening of competition in the STP market would likely have a significant negative impact on the quality and services provided to consumers. The probability that the proposed acquisition is unlawful is, as demonstrated above, substantial. The only harm the defendants would endure if preliminary relief is granted is delay, an equity that should be subordinated to the public’s interest in preserving the status quo until these issues are fully heard.

IV. Conclusion

In order to preserve competition in the market for submersible turbine pumps, the United States requests that this Court issue a temporary restraining order and a preliminary injunction to enjoin Franklin Electric, UDI, and United Dominion Industries Limited from consummating the

proposed joint venture pending a full trial on the merits.

Respectfully Submitted,

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